

ORIGINAL



0000146506

RECEIVED

BEFORE THE ARIZONA CORPORATION COMMISSION

2013 JUL 17 P 2:51

Arizona Corporation Commission

DOCKETED

JUL 17 2013

DOCKETED BY

nr

COMMISSIONERS

BOB STUMP, Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

AZ CORP COMMISSION
DOCKET CONTROL

IN THE MATTER OF THE APPLICATION OF THE
ARIZONA ELECTRIC POWER COOPERATIVE,
INC. FOR A HEARING TO DETERMINE THE
FAIR VALUE OF ITS PROPERTY FOR
RATEMAKING PURPOSES, TO FIX A JUST AND
REASONABLE RETURN THEREON AND TO
APPROVE RATES DESIGNED TO DEVELOP
SUCH RETURN

Docket No. E-01773A-12-0305

**AEPCO'S NOTICE OF FILING
REJOINDER TESTIMONY**

Pursuant to Procedural Orders dated September 11, 2012, March 5, 2013 and May 29,
2013 in this docket, attached are the Rejoinder Testimonies of Gary E. Pierson and Richard P.
Kurtz on behalf of the Arizona Electric Power Cooperative, Inc.

RESPECTFULLY SUBMITTED this 17th day of July, 2013.

GALLAGHER & KENNEDY, P.A.

By

Michael M. Grant
Jennifer A. Cranston
2575 East Camelback Road
Phoenix, Arizona 85016-9225
Attorneys for Arizona Electric Cooperative, Inc.

Original and 13 copies filed this
17th day of July, 2013, with:

Docket Control
Arizona Corporation Commission
1200 West Washington Street
Phoenix, Arizona 85007

1 **Copies** of the foregoing delivered
this 17th day of July, 2013, to:

2
3 Bridget Humphrey
4 Legal Division
5 Arizona Corporation Commission
6 1200 West Washington Street
7 Phoenix, Arizona 85007

8
9 Scott Hesla
10 Legal Division
11 Arizona Corporation Commission
12 1200 West Washington Street
13 Phoenix, Arizona 85007

14
15 Terri Ford
16 Utilities Division
17 Arizona Corporation Commission
18 1200 West Washington Street
19 Phoenix, Arizona 85007

20
21 Candrea Allen
22 Utilities Division
23 Arizona Corporation Commission
24 1200 West Washington Street
Phoenix, Arizona 85007

15 **Copies** of the foregoing mailed
this 17th day of July, 2013, to:

16 Michael W. Patten
17 Roshka DeWulf & Patten, PLC
18 One Arizona Center
19 400 East Van Buren Street, Suite 800
20 Phoenix, Arizona 85004
21 Attorneys for Trico Electric Cooperative, Inc.

22
23 Russell E. Jones
24 Waterfall, Economidis, Caldwell,
Hanshaw & Villamana P.C.
5210 East Williams Circle, Suite 800
Tucson, Arizona 85711
Attorneys for Trico Electric Cooperative, Inc.

1 Vincent Nitido
Karen Cathers
2 Trico Electric Cooperative, Inc.
8600 West Tangerine Road
3 P.O. Box 930
Marana, Arizona 85653
4
Jeffrey W. Crockett
5 Brownstein Hyatt Farber Schreck LLP
One East Washington Street, Suite 2400
6 Phoenix, Arizona 85004
Attorneys for Sulphur Springs Valley
7 Electric Cooperative, Inc.
8 Kirby Chapman
Surphur Springs Valley Electric
9 Cooperative, Inc.
311 East Wilcox Drive
10 Sierra Vista, Arizona 85635
11 Michael A. Curtis
William P. Sullivan
12 Curtis, Goodwin, Sullivan,
Udall & Schwab, P.L.C.
13 501 East Thomas Road
Phoenix, Arizona 85012-3205
14 Attorneys for Mohave Electric Cooperative, Inc.
15 Tyler Carlson
Mohave Electric Cooperative, Inc.
16 P.O. Box 1045
Bullhead City, Arizona 86430
17
Peggy Gillman
18 Mohave Electric Cooperative, Inc.
P.O. Box 1045
19 Bullhead City, Arizona 86430

20 

21 10421-67/3622493

22

23

24

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

BOB STUMP, Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

IN THE MATTER OF THE APPLICATION OF THE
ARIZONA ELECTRIC POWER COOPERATIVE,
INC. FOR A HEARING TO DETERMINE THE
FAIR VALUE OF ITS PROPERTY FOR
RATEMAKING PURPOSES, TO FIX A JUST AND
REASONABLE RETURN THEREON AND TO
APPROVE RATES DESIGNED TO DEVELOP
SUCH RETURN

Docket No. E-01773A-12-0305

Rejoinder Testimony of Gary E. Pierson

on Behalf of

Arizona Electric Power Cooperative, Inc.

General Rates Application

(Public Version)

July 17, 2013

TABLE OF CONTENTS

	<u>Page</u>
COST OF CAPITAL AND RATE SUFFICIENCY — AEP CO REJOINDER POSITION	1
COAL PROCUREMENT AND INVENTORY MANAGEMENT – AEP CO REJOINDER POSITION	4
ECAR TARIFF – AEP CO REJOINDER POSITION	6
SUMMARY OF AEP CO REJOINDER POSITION	8

1 **Q. Mr. Pierson, are you the same Gary E. Pierson who sponsored direct and rebuttal**
2 **testimony for Arizona Electric Power Cooperative, Inc. ("AEPCO") in this matter?**

3 **A. Yes, I am.**
4

5 **Q. Have you reviewed the surrebuttal testimonies of Staff witnesses Messrs. Vickroy,**
6 **Spangenberg, Kalbarczyk and Mazzini which were filed in this matter?**

7 **A. Yes, I have. My rejoinder testimony provides AEPCO's responses to certain issues**
8 **raised by Messrs. Vickroy, Kalbarczyk and Spangenberg. I also present recommended**
9 **revenue requirements and rates in support of and consistent with AEPCO's rejoinder**
10 **positions. Mr. Kurtz' rejoinder testimony will address key issues in Mr. Mazzini's**
11 **testimony.**
12

13 **COST OF CAPITAL AND RATE SUFFICIENCY — AEPCO REJOINDER POSITION**

14 **Q. Mr. Vickroy filed surrebuttal testimony on Staff's behalf presenting his response**
15 **and recommendations to AEPCO's rebuttal position regarding cost-of-capital and**
16 **rate sufficiency. Please provide the Company's response to Mr. Vickroy's**
17 **testimony.**

18 **A. AEPCO continues to recommend that its revenue requirements be established based upon**
19 **a debt service coverage ratio ("DSC") of 1.32. As shown by Exhibit REV-3 to**
20 **Mr. Vickroy's direct testimony, AEPCO's three-year historical average ratios (2010-**
21 **2012) fall within – and, in one case, exceed – the A-rated range of financial metrics for**
22 **electric generation and transmission cooperatives. Accordingly, AEPCO agrees with**
23 **Mr. Vickroy's direct testimony, which stated: "Based solely upon historical, quantitative**

1 metrics, AEPCO has produced financial results that could qualify it for an investment
2 grade rating. The financial metric qualifications in total comprise 40 percent of the
3 evaluation.”¹ AEPCO’s recommended 1.32 DSC falls mid-way between the range of
4 1.2x-1.4x as shown on Exhibit REV-3. Where we disagree is whether AEPCO’s qualitative
5 factors, which comprise 60 percent of the evaluation, also qualify the Cooperative for an
6 investment grade rating. For the reasons stated at pages 1-4 of my rebuttal testimony,
7 AEPCO believes that our risk levels fall within a normal range for an investment grade
8 rating. Therefore, given the fact that the quantitative and qualitative factors support an
9 investment grade rating, we continue to recommend revenue requirements be set based upon
10 a 1.32 DSC.

11
12 **Q. At page 2 of his surrebuttal testimony, Mr. Vickroy discusses the Supplement to**
13 **Petition for Administrative Reconsideration that AEPCO filed in late May of this**
14 **year with the Environmental Protection Agency. Mr. Vickroy questions whether**
15 **the EPA’s very prompt agreement to reconsider has reduced any of the risks**
16 **identified in Staff’s direct testimony. Please provide the Cooperative’s response.**

17 **A.** The EPA’s approval of our petition only nine days after we filed the Supplement is a very
18 strong, positive message that the EPA will act favorably on our proposed BART
19 alternative. As further evidence of that, the EPA has agreed that AEPCO should start the
20 process of modifying the State Implementation Plan to incorporate AEPCO’s proposed
21 BART alternative. Importantly, this development has greatly reduced AEPCO’s
22 construction build-risk exposure and addresses the concerns raised by Mr. Vickroy at

23 ¹ Vickroy Direct Testimony, p. 12, ll. 22-25.

1 page 14 of his direct testimony. Specifically, as I discussed at page 2 of my rebuttal
2 testimony, our BART alternative decreases the originally anticipated capital remediation
3 investment from an approximate \$190 million to a \$30 million level.
4

5 **Q. At page 3 of his surrebuttal testimony, Mr. Vickroy states that AEPCO's rates are**
6 **not competitive when compared to other utilities in the region. What is AEPCO's**
7 **position on this issue?**

8 A. For several years, AEPCO has been tracking its rates in comparison to the rates of other
9 utilities in the region and taking a variety of efficiency and cost-effective steps to
10 improve our competitiveness. These comparisons (which we shared with Staff during
11 discovery) show the improvements AEPCO has made over the years. Our recent victory
12 on rail rates, which led to a more than 20% decrease in delivered coal costs, is just one
13 example of our efforts and successes. As indicated in my rebuttal testimony at page 6,
14 the best way to continue AEPCO's progress regarding rate competitiveness is to grant our
15 request to lower our revenue requirements rather than to hold them steady as Mr. Vickroy
16 proposes.
17

18 **Q. Also at page 3 of his surrebuttal testimony, Mr. Vickroy suggests AEPCO**
19 **incorrectly contends that partial-requirements contracts do not carry more risk**
20 **than all-requirements contracts. Please respond.**

21 A. Although rating agencies may routinely assign more risk to generation cooperatives with
22 partial-requirements contracts, they primarily do so because of a concern that the
23 cooperative will not be able to recover its costs from partial-requirements members. This
24

1 rationale, however, does not apply to AEPCO, because our PRM contracts require
2 monthly fixed and O&M charges. These charges assure AEPCO's full recovery of its
3 fixed costs associated with serving each Member. Further, the fact that AEPCO is now
4 providing scheduling and trading services for two of its PRMs and, as a result, is more
5 familiar with their power needs should also remediate any negative perceptions regarding
6 PRM-related risks.

7
8 **Q. Does Mr. Vickroy's analysis of the Cooperative's risk profile alter AEPCO's**
9 **revenue requirements recommendation?**

10 **A.** No. AEPCO is confident that it does and will continue to rate positively on both the
11 quantitative and qualitative criteria. Since our last rate case, we have worked closely
12 with our Members to operate more efficiently and at lower costs. It is very appropriate to
13 pass along those savings to the Members and their retail customers. Therefore, we
14 continue to recommend that our revenue requirements should be based upon a 1.32 DSC.

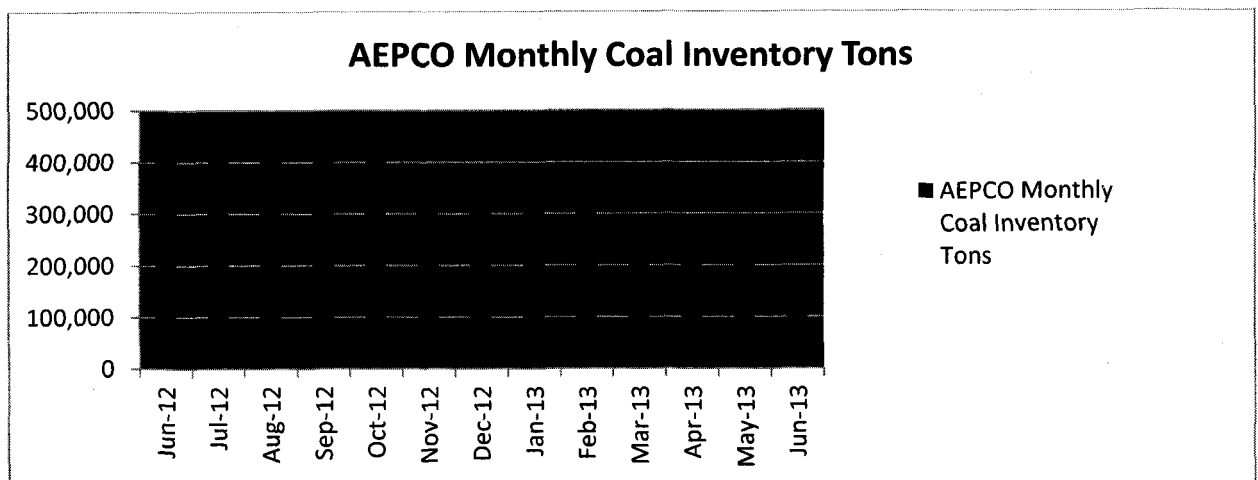
15
16 **COAL PROCUREMENT AND INVENTORY MANAGEMENT –**

17 **AEPCO REJOINDER POSITION**

18 **Q. Please provide the Company's response to Mr. Spangenberg's surrebuttal testimony**
19 **regarding AEPCO's coal forecasting, procurement and inventory management.**

20 **A.** Mr. Spangenberg's testimony indicates that AEPCO has avoided dealing with Liberty's
21 conclusions and recommendations on these topics. To the contrary, as indicated in my
22 rebuttal testimony at pages 12-13 and in the report provided by Ms. Regis, we have taken
23 and continue to take steps (1) to improve the accuracy of our coal forecasting and (2) to

1 bring our coal inventory within the target range. Our efforts have been successful, as
2 demonstrated by the fact that, as of June 26, our coal inventory is approximately [REDACTED]
3 tons, which is now, once again, within our target range. The chart below illustrates the
4 reduction of AEPCO's coal inventory from June 2012 to June 2013. It also shows that, in
5 just the past eight months, our inventory has been cut in half.



15 Additional evidence of the success of AEPCO's aggressive coal management strategy is
16 the fact that AEPCO has lowered its average delivered cost of coal by more than 20%
17 since our 2011 test year.

18
19 **Q. Mr. Spangenberg states that AEPCO's rebuttal testimony contains new information**
20 **and changed positions. Do you agree?**

21 **A.** No. Our rebuttal testimony is consistent with the information and data provided to
22 Liberty in response to more than 200 formal and informal data requests. As to
23 Mr. Spangenberg's specific example of a "revised position," the information in

1 Ms. Regis' report is entirely consistent with AEPCO's data request response in which we
2 explained that spot purchases accounted for the increase in inventory after March 2012.
3 As indicated in that same data request response, those spot purchases did not impact our
4 annual coal levels, which remained about the same at the beginning and end of 2012
5 ([REDACTED] tons as of 1/1/2012 compared to [REDACTED] tons as of 12/31/2012).
6

7 **Q. Does Mr. Spangenberg's testimony regarding AEPCO's coal supply practices**
8 **change the Cooperative's position?**

9 A. No. We still find Liberty's criticisms of our 2012 coal strategy misplaced. That being
10 said, we are in agreement regarding best practices going forward. AEPCO has been and
11 will continue to be committed to ensuring accuracy in its coal forecasting process and
12 aggressively managing its coal inventory for the benefit of its Members. Our success in
13 using the STB rail rate victory to lower coal costs and our ongoing reduction of our coal
14 inventory is firm evidence of that.
15

16 **ECAR TARIFF – AEPCO REJOINDER POSITION**

17 **Q. Staff's surrebuttal testimony recommends that AEPCO's revenue requirements be**
18 **held at test year levels and also recommends that the rate case be held open for**
19 **further consideration of AEPCO's proposed ECAR tariff. What is AEPCO's**
20 **reaction to these combined proposals?**

21 A. AEPCO offered the ECAR tariff in our rebuttal testimony in order to address Staff's
22 concerns about our ability to raise capital in response to future EPA compliance
23 requirements, particularly given our proposed revenue requirements decrease. The
24

1 ECAR was proposed under the assumption that AEPCO's rates would be based on a
2 lower DSC of 1.32. AEPCO does not believe that the ECAR is appropriate if Staff's
3 higher DSC recommendation is approved.
4

5 **Q. If the Commission approves AEPCO's request for rates based on a 1.32 DSC, what**
6 **is the Cooperative's position regarding Mr. Kalbarczyk's proposal that the rate case**
7 **be held open to continue discussions with Staff regarding the ECAR mechanism?**

8 A. Under that assumption, AEPCO agrees that the docket should be held open. We will
9 work with Staff to develop the process for, and details of, the ECAR mechanism.
10

11 **Q. At page 6 of his surrebuttal testimony, Mr. Kalbarczyk suggests that the ECAR**
12 **should be set at zero until AEPCO's completion of an economic study of Apache**
13 **Station. Please provide the Cooperative's response to this proposal.**

14 A. After receiving Staff's surrebuttal testimony, AEPCO met with Staff to try to gain a
15 better understanding of the kind of study being suggested and how it will relate to the
16 ECAR mechanism. While we were not able to reach complete agreement with Staff on
17 the details and conditions associated with the study, the discussion did assist us in
18 refining our study proposal. We request that the Commission approve the following
19 process as compliant with any study requirement.
20

21 Specifically, the study by our Strategic Resource Planning Group ("SRPG") (which has
22 already begun) involves a detailed comparison of the continued operations of Steam
23 Turbines 2 and 3 under AEPCO's BART proposal with a mix of other Apache resource
24

1 supply options/modifications, including, but not limited to, different operating
2 configurations of the two steam turbine units; construction of new natural gas-fired
3 resources; and replacement purchased power agreements ("PPA") with associated
4 transmission upgrades. The study will examine the impacts of these and other scenarios
5 on operating costs, capital requirements, stranded investment and unit retirement costs.
6 We will also conduct a Request for Proposal or similar process to verify market
7 assumptions and long-term PPA market costs. The foregoing information will then be
8 used by AEPCO in preparing financial forecasts and rate projections. The results of these
9 various analyses will be submitted to the Commission – including a non-confidential
10 executive summary that can be made available to the public – on or before June 30, 2014.
11 Our discussions with Staff regarding ECAR details can proceed while the study is being
12 conducted. The ECAR, once approved by the Commission, should be set at zero until the
13 study is submitted and an appropriate ECS is developed.

14 15 **SUMMARY OF AEPCO REJOINDER POSITION**

16 **Q. Mr. Pierson, please summarize AEPCO's rejoinder position.**

17 A. AEPCO's rejoinder position regarding operating income and rate design is the same as
18 presented in our rebuttal testimony. Specifically, we request that the Commission authorize
19 a reduction in our revenues of approximately \$4.3 million instead of Staff's proposal of no
20 change. For ease of reference, my Exhibit GEP-9 summarizes AEPCO's original rate filing,
21 Staff's direct testimony, AEPCO's rebuttal, Staff's surrebuttal and AEPCO's rejoinder
22 positions.

1 AEPCO and Staff agree on rate design, although our proposed rates differ because of our
2 different positions on DSC. My Exhibit GEP-10 summarizes AEPCO's current rates, its
3 filed rates, Staff's direct proposed rates, AEPCO's rebuttal proposed rates, Staff's
4 surrebuttal proposed rates and AEPCO's rejoinder proposed rates. We request that the
5 rates shown in column 6 of Exhibit GEP-10 be approved to go into effect on
6 November 1, 2013.

7
8 If the Commission approves the revenue requirement proposed by AEPCO, then we also
9 request that the Commission hold open this docket for Staff and AEPCO to bring back to
10 the Commission a joint recommendation on, and a request for approval of, an ECAR
11 tariff and plan of administration.

12
13 We also request that the Commission approve the SRPG planning process which
14 Mr. Kurtz and I have described in our rejoinder testimonies.

15
16 Finally, AEPCO requests (1) its Purchased Power Fuel Adjustor Clause be continued
17 with the revisions discussed in my direct and rebuttal testimonies, as well as (2) approval
18 of the depreciation rates stated in Exhibit PS-2 to Mr. Scott's direct testimony.

19
20 **Q. Does this conclude your rejoinder testimony?**

21 **A.** Yes, it does.
22
23

EXHIBIT GEP-9

Arizona Electric Power Cooperative, Inc.
Comparison of Increase in Gross Revenue Requirement
Test Year Ended December 31, 2011

Line No.	Description	Col. A Company As Filed Position	Col. B Staff Direct Position	Col. C Company Rebuttal Position	Col. D Staff Surrebuttal Position	Col. E Company Rejoinder Position
1	Summary of Revenue Increase Proposed:					
2	Proposed Revenue Increase	\$ (4,527,467)	\$ -	\$ (4,287,465)	\$ -	\$ (4,287,465)
3	Revenues in Test Year - Present Rates	\$ 154,924,873	\$ 154,924,871	\$ 154,924,871	\$ 154,924,871	\$ 154,924,871
3	Revenue Increase Percentage	-2.92%	0.00%	-2.77%	0.00%	-2.77%
4						
5	Pro Forma Statement of Operations					
6	with Proposed Rates:					
7	Operating Revenues	\$ 159,097,135	\$ 163,624,600	\$ 159,337,135	\$ 163,624,600	\$ 159,337,135
8	Operating Expense	148,420,479	148,420,479	148,660,479	148,660,479	148,660,479
9	Electric Operating Margins	10,676,656	15,204,121	10,676,656	14,964,121	10,676,656
10	Interest & Other Deductions	9,745,481	9,745,481	9,745,481	9,745,481	9,745,481
11	Operating Margins	931,175	5,458,640	931,175	5,218,640	931,175
12	Non-Operating Margins	1,026,046	1,026,046	1,026,046	1,026,046	1,026,046
13	Net Patronage Capital or Margins	\$ 1,957,221	\$ 6,484,686	\$ 1,957,221	\$ 6,244,686	\$ 1,957,221
14						
15	Times Interest Earned Ratio:					
16	Net Patronage Capital or Margins	\$ 1,957,221	\$ 6,484,686	\$ 1,957,221	\$ 6,244,686	\$ 1,957,221
17	Interest on Long Term Debt	9,281,871	9,281,871	9,281,871	9,281,871	9,281,871
18	Total	\$ 11,239,092	\$ 15,766,557	\$ 11,239,092	\$ 15,526,557	\$ 11,239,092
19	Times Interest Earned Ratio	1.21	1.70	1.21	1.67	1.21
20						
21	Debt Service Coverage Ratio:					
22	Net Patronage Capital or Margins	\$ 1,957,221	\$ 6,484,686	\$ 1,957,221	\$ 6,244,686	\$ 1,957,221
23	Depreciation & Amortization	13,349,504	13,349,504	13,349,504	13,349,504	13,349,504
24	Interest on Long Term Debt	9,281,871	9,281,871	9,281,871	9,281,871	9,281,871
25	Total	\$ 24,588,596	\$ 29,116,061	\$ 24,588,596	\$ 28,876,061	\$ 24,588,596
26						
27	Interest on Long Term Debt	\$ 9,281,871	\$ 9,281,871	\$ 9,281,871	\$ 9,281,871	\$ 9,281,871
28	Principal Payments	9,345,853	9,345,853	9,345,853	9,345,853	9,345,853
29	Debt Service	\$ 18,627,724	\$ 18,627,724	\$ 18,627,724	\$ 18,627,724	\$ 18,627,724
30	Debt Service Coverage Ratio	1.32	1.56	1.32	1.55	1.32
31						
32	Return on Fair Value Rate Base:					
33	Electric Operating Margins	\$ 10,676,656	\$ 15,204,121	\$ 10,676,656	\$ 14,964,121	\$ 10,676,656
34	Rate Base	\$ 267,463,587	\$ 261,075,032	\$ 261,075,032	\$ 261,075,032	\$ 261,075,032
35	Return on Fair Value Rate Base	3.99%	5.82%	4.09%	5.73%	4.09%

References:

38 Column A: Company Original Filed Schedules

39 Column B: Company Rebuttal Testimony and Schedules

40

Column B: Staff Direct Testimony and Schedules

Column D: Kalbarczyk Surrebuttal Testimony and Exhibits

EXHIBIT GEP-10

Arizona Electric Power Cooperative, Inc.
Comparison of Proposed Rates & PPFAC Bases and Proof of Revenues
Test Year Ended December 31, 2011

Line	Description	Col. 1		Col. 2		Col. 3		Col. 4		Col. 5		Col. 6	
		Company Current Rates	Position	Company As Filed	Position	Staff Direct	Position	Company Rebuttal	Position	Staff Surrebuttal	Position	Company Rejoinder	Position
1	<u>Collective All-Requirements Members: (1)</u>												
2	Fixed Charge - \$/Month	\$ 273,334	\$	280,598	\$	320,713	\$	280,682	\$	318,671	\$	280,682	\$
3	O&M Charge - \$/Month	\$ 414,019	\$	458,175	\$	458,175	\$	462,845	\$	462,842	\$	462,845	\$
4	Energy Rates:												
5	Base Resources \$/kWh	\$ 0.03132	\$	0.02921	\$	0.02921	\$	0.02958	\$	0.02946	\$	0.02958	\$
6	Other Existing Resources \$/kWh	\$ 0.05300	\$	0.04795	\$	0.04795	\$	0.03904	\$	0.04119	\$	0.03904	\$
7	PPFAC Bases:												
8	PPFAC-Base Resources Base - Per kWh	\$ 0.03513	\$	0.02921	\$	0.02921	\$	0.02958	\$	0.02946	\$	0.02958	\$
9	PPFAC-Other Resources Base - Per kWh	\$ 0.07188	\$	0.04795	\$	0.04795	\$	0.03904	\$	0.04119	\$	0.03904	\$
10	PPFAC-Fixed Fuel Costs Base - Per Month	\$ -	\$	180,956	\$	180,956	\$	183,236	\$	183,236	\$	183,236	\$
11	Revenues Generated	\$ 16,903,585	\$	16,684,166	\$	17,165,549	\$	16,630,822	\$	17,106,439	\$	16,630,822	\$
12	Revenue Increase over Current Rates	\$	\$	(219,419)	\$	261,964	\$	(272,763)	\$	202,854	\$	(272,763)	\$
13	Percentage Increase (Decrease)			-1.30%		1.55%		-1.61%		1.20%		-1.61%	
14													
15	<u>Partial-Requirements Members:</u>												
16	<u>Mohave Electric Cooperative</u>												
17	Fixed Charge - \$/Month	\$ 835,756	\$	856,355	\$	978,782	\$	856,617	\$	972,557	\$	856,617	\$
18	O&M Charge - \$/Month	\$ 1,274,882	\$	1,419,059	\$	1,419,059	\$	1,433,723	\$	1,433,715	\$	1,433,723	\$
19	Energy Rates:												
20	Base Resources \$/kWh	\$ 0.03191	\$	0.02894	\$	0.02894	\$	0.02931	\$	0.02919	\$	0.02931	\$
21	Other Existing Resources \$/kWh	\$ 0.05852	\$	0.05437	\$	0.05437	\$	0.04118	\$	0.04436	\$	0.04118	\$
22	PPFAC Bases:												
23	PPFAC-Base Resources Base - Per kWh	\$ 0.03454	\$	0.02894	\$	0.02894	\$	0.02931	\$	0.02919	\$	0.02931	\$
24	PPFAC-Other Resources Base - Per kWh	\$ 0.06191	\$	0.05437	\$	0.05437	\$	0.04118	\$	0.04436	\$	0.04118	\$
25	PPFAC-Fixed Fuel Costs Base - Per Month	\$ -	\$	542,273	\$	542,273	\$	549,433	\$	549,433	\$	549,433	\$
26	Revenues Generated	\$ 50,184,760	\$	46,950,488	\$	48,419,615	\$	47,374,155	\$	48,686,609	\$	47,374,155	\$
27	Revenue Increase over Current Rates	\$	\$	(3,234,272)	\$	(1,765,145)	\$	(2,810,605)	\$	(1,498,151)	\$	(2,810,605)	\$
28	Percentage Increase (Decrease)			-6.44%		-3.52%		-5.60%		-2.99%		-5.60%	
29													

Arizona Electric Power Cooperative, Inc.
Comparison of Proposed Rates & PPFAC Bases and Proof of Revenues
Test Year Ended December 31, 2011

Line	Description	Col. 1		Col. 2		Col. 3		Col. 4		Col. 5		Col. 6	
		Company	Current	Company	As Filed	Staff	Direct	Company	Rebuttal	Staff	Surrebuttal	Company	Rejoinder
		Rates		Position	Position	Position	Position	Position	Position	Position	Position	Position	Position
1	<u>Sulphur Springs Valley Electric Cooperative</u>												
2	Fixed Charge - \$/Month	\$	740,041	\$	758,281	\$	866,687	\$	758,513	\$	861,175	\$	758,513
3	O&M Charge - \$/Month	\$	1,128,876	\$	1,256,541	\$	1,256,541	\$	1,269,525	\$	1,269,518	\$	1,269,525
4	Energy Rates:												
5	Base Resources \$/kWh	\$	0.03205	\$	0.02938	\$	0.02938	\$	0.02975	\$	0.02963	\$	0.02975
6	Other Existing Resources \$/kWh	\$	0.05742	\$	0.05109	\$	0.05109	\$	0.04139	\$	0.04373	\$	0.04139
7	PPFAC Bases:												
8	PPFAC-Base Resources Base - Per kWh	\$	0.03449	\$	0.02938	\$	0.02938	\$	0.02975	\$	0.02963	\$	0.02975
9	PPFAC-Other Resources Base - Per kWh	\$	0.06449	\$	0.05109	\$	0.05109	\$	0.04139	\$	0.04373	\$	0.04139
10	PPFAC-Fixed Fuel Costs Base - Per Month	\$	-	\$	480,169	\$	480,169	\$	486,509	\$	486,509	\$	486,509
11	Revenues Generated	\$	47,411,111	\$	45,317,701	\$	46,618,576	\$	45,736,988	\$	46,885,038	\$	45,736,988
12	Revenue Increase over Current Rates			\$	(2,093,410)	\$	(792,535)	\$	(1,674,122)	\$	(526,073)	\$	(1,674,122)
13	Percentage Increase (Decrease)				-4.42%		-1.67%		-3.53%		-1.11%		-3.53%
14													
15	<u>Trico Electric Cooperative</u>												
16	Fixed Charge - \$/Month	\$	710,367	\$	743,828	\$	850,168	\$	743,980	\$	844,676	\$	743,980
17	O&M Charge - \$/Month	\$	764,465	\$	859,840	\$	859,840	\$	868,482	\$	868,478	\$	868,482
18	Energy Rates:												
19	Base Resources \$/kWh	\$	0.03214	\$	0.02947	\$	0.02947	\$	0.02984	\$	0.02972	\$	0.02984
20	Other Existing Resources \$/kWh	\$	0.05747	\$	0.04219	\$	0.04219	\$	0.03747	\$	0.03861	\$	0.03747
21	PPFAC Bases:												
22	PPFAC-Base Resources Base - Per kWh	\$	0.03431	\$	0.02947	\$	0.02947	\$	0.02984	\$	0.02972	\$	0.02984
23	PPFAC-Other Resources Base - Per kWh	\$	0.08274	\$	0.04219	\$	0.04219	\$	0.03747	\$	0.03861	\$	0.03747
24	PPFAC-Fixed Fuel Costs Base - Per Month	\$	-	\$	569,977	\$	569,977	\$	574,197	\$	574,197	\$	574,197
25	Revenues Generated	\$	40,425,414	\$	41,445,050	\$	42,721,131	\$	40,895,440	\$	42,246,784	\$	40,895,440
26	Revenue Increase over Current Rates			\$	1,019,636	\$	2,295,717	\$	470,026	\$	1,821,370	\$	470,026
27	Percentage Increase (Decrease)				2.52%		5.68%		1.16%		4.51%		1.16%
28													
29	Total Revenues Generated	\$	154,924,871	\$	150,397,405	\$	154,924,871	\$	150,637,406	\$	154,924,870	\$	150,637,406
30	Total Revenue Increase over Current Rates			\$	(4,527,466)	\$	0	\$	(4,287,465)	\$	(1)	\$	(4,287,465)
31	Percentage Increase (Decrease)				-2.92%		0.00%		-2.77%		0.00%		-2.77%
32													

1) The Fixed Charge and the O&M Charge will be apportioned among the CARMs based upon each CARM's monthly Demand Ratio Share.

BEFORE THE ARIZONA CORPORATION COMMISSION

COMMISSIONERS

BOB STUMP, Chairman
GARY PIERCE
BRENDA BURNS
BOB BURNS
SUSAN BITTER SMITH

IN THE MATTER OF THE APPLICATION OF THE
ARIZONA ELECTRIC POWER COOPERATIVE,
INC. FOR A HEARING TO DETERMINE THE
FAIR VALUE OF ITS PROPERTY FOR
RATEMAKING PURPOSES, TO FIX A JUST AND
REASONABLE RETURN THEREON AND TO
APPROVE RATES DESIGNED TO DEVELOP
SUCH RETURN

Docket No. E-01773A-12-0305

Rejoinder Testimony of Richard P. Kurtz

on Behalf of

Arizona Electric Power Cooperative, Inc.

General Rates Application

July 17, 2013

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24

TABLE OF CONTENTS

Page

APACHE STATION – AEPCO REJOINDER POSITION 1

ECONOMIC STUDY RECOMMENDATION – AEPCO REJOINDER POSITION 4

SUMMARY OF AEPCO REJOINDER POSITION 7

1 **Q. Mr. Kurtz, are you the same Richard Kurtz who sponsored rebuttal testimony for**
2 **Arizona Electric Power Cooperative, Inc. ("AEPCO") in this matter?**

3 **A. Yes, I am.**
4

5 **Q. Have you reviewed the surrebuttal testimony of Staff witness Richard Mazzini filed**
6 **in this matter on July 3, 2012?**

7 **A. Yes, I have. My rejoinder testimony provides AEPCO's response to certain issues raised**
8 **in Mr. Mazzini's surrebuttal testimony.**
9

10 **APACHE STATION – AEPCO REJOINDER POSITION**

11 **Q. At pages 1-2 of his surrebuttal testimony, Mr. Mazzini reiterates his conclusion that**
12 **Apache Station Units ST2 and ST3 have been in decline for a number of years and**
13 **that there is no reasonable basis to believe that the decline has ended. Please**
14 **provide the Cooperative's response.**

15 **A. AEPCO continues to disagree with Mr. Mazzini's assessment of Apache Station and,**
16 **specifically, his claims regarding the reasons for the decline in ST2 and ST3 usage. As**
17 **detailed and documented in my rebuttal testimony and report, the output concerns raised**
18 **by Mr. Mazzini are linked to specific, external and non-reoccurring causes, the most**
19 **significant of which were the expiration of the SRP contract at the end of 2010 and high**
20 **coal costs relative to market energy prices.**

21
22 **AEPCO also disagrees with Mr. Mazzini's dismissal of the significant increase in station**
23 **output which we have experienced in 2013. The coal burn statistics provided in my**

1 rebuttal show that the combined output from ST2 and ST3 in the first four months of
2 2013 is at a five-year high; *i.e.*, it exceeds the January through April coal burn for these
3 units from each of the prior four years. This evidence of the continued viability of the
4 coal units is further supported by the market forecasts we have received from our expert
5 consultants. These analyses indicate that our coal-fired units will remain competitive to
6 the market for at least the next several years.

7
8 **Q. What is the Cooperative's response to Mr. Mazzini's testimony at page 3 regarding**
9 **the capacity value of Apache Unit ST1 (CC1)?**

10 A. Mr. Mazzini claims that AEPCO has failed to provide a definitive and quantitative
11 explanation of how CC1 has value as capacity. Among other things, this argument
12 ignores AEPCO's 2010 economic analysis of CC1, which was endorsed by Liberty in
13 AEPCO's last rate case:

14 **Experience and recent management study confirm the continuing**
15 **usefulness of CC1 and the gas turbine units.**

16 ...

17 Management's April 5, 2010 study examined future options, concluding
18 that continued use of CC1 for reserve and seasonal peaking capacity
19 remained AEPCO's most economic alternative. The study's conclusions
may seem surprising based on recent unit performance, but appear more
credible from a longer-term perspective.

20 Exhibit RPK 3-3 (Liberty Public Report, July 30, 2010, page 72) (bolding in original)
21 (underline added).

1 Since 2010, AEPCO has continued to evaluate the role of CC1 in meeting Member needs
2 by comparing its costs to substitute capacity available on the market. As stated in my
3 rebuttal report at page 12, in 2012, the yearly capacity cost for CC1 was only \$28.30 per
4 kW compared to the \$37.80 per kW six-month demand rate for one of AEPCO's
5 Purchase Power Agreements ("PPA"). Further, comparing projected costs provides
6 additional, quantitative evidence of CC1's value as capacity. The projected capacity cost
7 for CC1 in 2015 is \$1.78 per kW-month. That is significantly less than the PPA
8 agreements currently in place, which have projected 2015 demand rates of \$8.85 per kW-
9 month and \$10.58 per kW-month. Thus, the "capacity value" of CC1 is a savings of
10 more than \$500,000 per month in avoided capacity charges when AEPCO, instead,
11 purchases real-time market energy against CC1.

12
13 **Q. Is there any other information relevant to the issue of ST1's continued usefulness to**
14 **AEPCO?**

15 A. Yes. I indicated at page 9 of my rebuttal report that, historically, we have operated CC1
16 during the summer months when and as needed to cover peak load. In fact, we used CC1
17 in this operational role just a few weeks ago. In late June, AEPCO placed CC1 in service
18 for six days. During this time, CC1 and the other Apache gas-fired combustion turbines
19 ran at high capacity factors during peak hours when market energy costs exceeded our
20 production costs. During off-peak hours, when market energy costs were low, the
21 combustion turbines were taken off-line and CC1 was backed down to minimum loads.
22 The calculated cost savings of operating these units, including CC1, during the peak
23

1 hours was nearly \$300,000 and the savings amounted to more than \$100,000 when
2 compared to day-ahead block and real-time market energy purchases.
3

4 **Q. Does Mr. Mazzini's discussion of Apache Station in his surrebuttal testimony**
5 **change AEPCO's position regarding Apache's historic operation and continued**
6 **use?**

7 A. No. The data and analysis in my rebuttal testimony and report explain fully the unique
8 factors that caused the output decline from the coal-fired units in 2009, 2011 and 2012:
9 (1) high coal prices (which have now been rectified by the STB ruling and our successful
10 coal cost negotiation efforts) combined with low market prices and (2) the scheduled
11 expiration of SRP's 100 MW, 20-year sales contract. ST2 and ST3 are now operating
12 and are expected to continue to operate over the next several years at much higher levels.
13 Further, CC1 has considerable, long-term value based on the capacity value analysis and
14 cost savings calculations discussed in my rebuttal and rejoinder testimonies – the validity
15 of which was most recently confirmed by CC1's cost-savings operations about two weeks
16 ago.
17

18 **ECONOMIC STUDY RECOMMENDATION – AEPCO REJOINDER POSITION**

19 **Q. Staff's surrebuttal testimony includes a recommendation that AEPCO conduct an**
20 **economic study of Apache Station. Please provide the Cooperative's response to**
21 **this proposal.**

22 A. As discussed in Mr. Pierson's rejoinder testimony, after receiving Staff's surrebuttal
23 testimony, AEPCO met with Staff to gain a better understanding of the kind of study
24

1 being suggested. Although we do not agree with Staff on certain details and conditions
2 associated with the study, I will describe the analysis of Apache Station our Strategic
3 Resource Planning Group ("SRPG") has already commenced and which we propose to
4 continue and complete as our Apache Study in compliance with this study
5 recommendation.

6
7 **Q. Please describe the work of the SRPG.**

8 A. The SRPG is comprised of highly qualified AEPCO staff, outside consultants and
9 Member Cooperative personnel. The SRPG and its Technical Team are in the process of
10 conducting a comprehensive study ("SRPG Study") analyzing the future of Apache
11 Station's viable operations.

12
13 The first stage of the SRPG Study commenced with a detailed comparison of the
14 operating costs, capital requirements and potential stranded costs associated with a
15 variety of resource alternatives to Apache Station's current configuration and uses.
16 AEPCO hired Burns & McDonnell to use Strategist, a Ventyx product, to analyze a
17 number of different resource configurations, including analysis of the viability of
18 Apache's existing fleet with environmental upgrades under the following scenarios:

- 19 1) AEPCO's alternative BART proposal submitted to the EPA (installing
20 Selective Non-Catalytic Reduction on ST3 burning coal and
21 converting ST2 to burn natural gas only); or
22 2) Installing Selective Catalytic Reduction on ST2 and ST3 while
23 burning coal; or

1 3) Converting both ST2 and ST3 to burn natural gas only; or

2 4) Shutting down ST2 and/or ST3.

3 Burns & McDonnell's analysis also looks at construction of new natural gas-fired
4 resources at Apache, as well as the possible use of PPAs (with any necessary
5 transmission upgrades) as substitution options for Apache units.

6
7 The Strategist modeling is based, in part, on market data from Wood Mackenzie and
8 ACES regarding forward market energy and fuel forecasts. Initial Strategist modeling
9 results indicate that continued use of the Apache units under AEPCO's alternative BART
10 proposal to the EPA has the lowest net present value utility cost when compared to
11 procuring other resource alternatives to serve AEPCO's load obligations.

12
13 In conjunction with the Strategist modeling, the SRPG will also conduct a full unit
14 retirement analysis by which they will evaluate stranded investment, operational changes
15 and decommissioning costs in connection with potential unit retirement. The SRPG will
16 also conduct a Request for Proposal or similar public request for information process in
17 order to compare market power costs against the market assumptions utilized in the
18 Strategist modeling and as an additional verification of AEPCO's long-term PPA market
19 costs and CC1 capacity value. The SRPG will then use the results of these various
20 analyses as the basis for Planning & Risk (PaR) models (another Ventyx product) to
21 provide variable cost projections for financial forecasting and rate projections.

1 Finally, the results of these analyses will be provided to the Commission – together with
2 a non-confidential executive summary which can be made publicly available – on or
3 before June 30, 2014.
4

5 **SUMMARY OF AEPCO REJOINDER POSITION**

6 **Q. Mr. Kurtz, please summarize AEPCO's rejoinder position as it relates to the**
7 **subjects addressed in your testimony.**

8 A. AEPCO has demonstrated the current viability of Apache Station and provided data that
9 supports the useful lives of its units ST1, ST2 and ST3. As to Liberty's recommendation
10 regarding a study of Apache Station, as discussed last week with Staff, AEPCO proposes
11 the Commission approve the SRPG planning process as described herein.
12

13 **Q. Does this conclude your rejoinder testimony?**

14 A. Yes, it does.
15
16
17
18
19
20
21
22
23